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Supreme Court, U.S.
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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1991

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2 TUDOR CITY
PLACE ASSOCIATES
and 2 TUDOR GARDEN
PARKING CORPORATION,

Petitioners,

-against-

2 TUDOR CITY
TENANTS CORPORATION,
KINNEY SYSTEMS, INC. and
AMERICAN SAVINGS BANK,

Respondent.

PETITIONER'S REPLY TO THE BRIEF FOR RESPONDENT IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI

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ARGUMENT

This case presents an issue of statutory construction with both practical and theoretical importance. At the practical level, the success or failure of condominium and cooperative conversions may depend on whether tenant organizations are allowed to terminate, without cause, certain economically desirable and above board leases under the Condominium and Cooperative Abuse Relief Act, 15 U.S.C. §3601 et seq. (the "Act"). Theoretically, the case raises the issue of how a federal court should interpret a federal statute that governs an area that Congress itself believed should be regulated largely by the states. The Second Circuit twisted the language of the Act in order to expand the scope of its coverage.

Granting certiorari in this case, therefore, provides this Court with a perfect vehicle to develop principles for interpreting imprecisely drafted federal statutes intended to preserve the dominant state regulatory role.

Petitioners 2 Tudor City Place Associates ("Associates") and 2 Tudor Garden Parking Corp. ("Parking") submit this Reply Brief for two purposes. First, to redirect the Court to the important issues of statutory construction unfairly obscured in the Brief in Opposition of respondent 2 Tudor City Tenants Corp. ("Tenants"), and, second, to show the irrelevance to those issues of the factual controversies injected by Tenants in its Brief.

Tenants has carefully constructed its Brief in Opposition to create the false impression that it is composed of

weak and gullible unit holders who have been fooled by petitioners' machinations. But this is not a case that involves unsophisticated tenants at the mercy of skilled and unscrupulous developers. Respondent was at all times represented by sophisticated counsel who took advantage of the extensive legal protection provided to tenants in conversion projects, and who bargained hard to obtain the best possible deal for themselves under the relevant substantive law.

This case, therefore, does not involve tenant-victims of economic exploitation, but rather a strained and contrived judicial interpretation of the Condominium and Cooperative Abuse Relief Act that has allowed a sophisticated tenants group to reap an enormous economic windfall without any

statutory or economic justification.

I. RESPONDENT HAS FAILED TO ADDRESS ANY OF THE LEGAL ISSUES RAISED IN THE PETITION FOR CERTIORARI

Tenants utterly fails to confront the internal difficulties with the Condominium and Cooperative Abuse Relief Act, its legislative history, and its unsound interpretation in the Second Circuit. To read Tenants' account of the Act, one would think that section 3607, the subject of this litigation, was the centerpiece of the Act, and that section 3608, which dealt with setting aside unconscionable leases entered into before June 4, 1975, was a casual afterthought. Both the Act itself and its legislative history belie that interpretation.

Section 3608, which sets out elaborate tests to determine when unconscionable leases may be set aside, was subject to extensive debate and

compromise between the Senate, which wanted tougher controls, and the House of Representatives, which wanted to leave this matter largely in the hands of the states. The great anomaly of the Act is that the legislative history contains virtually no discussion of section 3607, even though it provided tenants with a future self-help remedy that was far more intrusive into state law. Congress never indicated why this extraordinary relief was needed or how it would work in individual cases.

When Congress intends to confer on any group of persons the power to unilaterally terminate a contractual arrangement, it should surely give clear notice of the set of transactions covered so that interested and informed parties can steer clear of any statutory trapdoor. Yet here Congress gave neither clue as to why this

extraordinary remedy was needed nor any indication of the remedy's scope. The Second Circuit's construction of the Act to cover leases for garage space upset virtually everyone's initial and legitimate expectations of the Act's reach.

Owing to the Congressional uneasiness and uncertainty about the scope of the Act, the Second Circuit should have exercised judicial prudence in construing section 3607, and not have stretched the language of the Act to nullify commercially useful and above-board transactions. But as our Petition for Certiorari demonstrates, the Second Circuit made two unwarranted leaps.

First, the Second Circuit assumed that, in general, all leases were contracts covered by section 3607, and, in particular, that this Garage Lease

was a contract for the "operation, maintenance, or management" of property serving the cooperative, even though this Garage Lease imposed no service obligations on Parking, as tenant, but allowed it to either leave the space unoccupied or use it for any other purpose, so long as it paid the rent stipulated in the Lease.

More importantly, the Second Circuit misconstrued section 3607 to cover transactions that did not involve "self-dealing." Although Tenants profess to find petitioners' arguments about the reach of section 3607 "incomprehensible" (Respondents Brief at page 27), it offers no reason why those arguments are incorrect. Instead, Tenants takes an irresponsible, know-nothing approach to section 3607, asserting that "control is control, whether it is 100% or 51%."

(Respondent's Brief at 27) That is wrong on every count.

The importance of divided control, while derided by Tenants, is explicitly recognized in section 3607, which is officially titled, "Termination of Self-Dealing Contracts." "Self-dealing," as ordinarily understood, can only occur when the same party is on both sides of the transaction in unequal proportions. Some other party must have an interest at risk on one side of the transaction in order for self-dealing to occur. Self-dealing cannot occur when the same persons are in 100 percent control of both sides of the deal. The Second Circuit was simply wrong to describe any pre-conversion contract or lease as a self-dealing arrangement (A-7), even in the absence of divided control.

Congress plainly intended this

ordinary sense of self-dealing to control. Section 3607(c) makes it clear that only those contracts entered into "while" the developer had "special developer control," or a majority of the votes of the association, are covered by section 3607. The definition of "special developer control" in section 3603(22), which elaborates on which shares count toward the developer's control, only makes sense in the context of divided ownership. There is no "special developer control" when the developer owns all the shares; no one cares how power is allocated between shares when all are owned by the same person.

When the Second Circuit erroneously paraphrased section 3607(c) to say that it allowed tenants to set aside any transaction entered into "prior to the time" tenants took over

the control of the cooperative board, it read the self-dealing requirements out of the Act. In the absence of clear indication to the contrary, the Second Circuit should have adhered to the ordinary meaning of self-dealing and limited the potential reach of section 3607's extraordinary remedial provision. By extending that reach, the Second Circuit has ignored Congress' intent and committed a major blunder of statutory construction that this Court should correct.

II. RESPONDENT HAS INJECTED INTO ITS STATEMENT MISLEADING AND IRRELEVANT FACTS THAT DEFLECT THIS COURT FROM THE IMPORTANT LEGAL ISSUES RAISED IN THIS CASE

A. The Present Suit Involves No Issue Of Misrepresentation or Nondisclosure

Throughout it brief, Tenants repeatedly refers to alleged failures to disclose pertinent information about

the Garage Lease in the conversion offering materials. But this case does not involve fraud, misrepresentation, concealment, nondisclosure or violation of the blue sky or federal securities law. Tenants, like anyone else, might have elected to bring an action for any of these forms of wrongful conduct under either state or federal law. But then it would have had to prove the falsity of the statements made, their materiality, and their causal connection to any relevant loss. As even Tenants recognizes, it is most unlikely that it would prevail, given the courts' unwillingness to upset similar leases without recourse to section 3607 of the Act. (Respondent's Brief, p.21, n.2)

In any event, Tenants' entirely unsupported allegations of nondisclosure and misrepresentation are

wholly beside the point. Under the Act as the Second Circuit has read it, Tenants could set aside the Garage Lease even if the unit holders had perfect knowledge of its terms and conditions, and had solemnly agreed to abide by all of them. Indeed, that is precisely the holding of West 14th Street Commercial Corp. v. 5 West 14th Street Owners Corp., 815 F.2d 188 (2d Cir. 1987), cert. denied, 484 U.S. 850 (1987), which allowed tenants to set aside a lease, even though its terms had been the subject of exhaustive negotiations.

The only question presented by this case is whether the naked power granted to Tenants under the Act extended to the Garage Lease entered in well before the conversion process began.

B. The Present Suit Involves No Issue Of Excessive Rate Of Return

Tenants also claims, as if it were proven facts, that Associates made a profit on the conversion even without the Garage Lease, that prices for individual units were not lowered to reflect the anticipated profits of that lease, and that 124 units in the original offering constituted an economic asset left out of petitioners' accounting. These issues, too, are irrelevant to the present suit, which does not involve any form of rate of return regulation on the developer.

Moreover, even if Associates did derive profit from the conversion deal apart from the Garage Lease -- which petitioners would vigorously contest in any proceeding in which it were relevant -- Tenants still has offered no reason why it should be able to grab those profits for itself. Under the

Second Circuit's interpretation, Tenants could unilaterally set aside the Garage Lease even if it plunged Associates into instant bankruptcy.

C. The Present Suit Involves No Issue Of Hardship Relief For Tenants

Tenants also complains that in "difficult" economic times it is hard for tenants to meet rising expenses on limited incomes. (Respondent's Brief, at 24) But bad times and rising costs afflict landlords as well as tenants, and so long as tenants reap the benefits of prudent purchases in boom times, they should not be allowed to undo in whole or in part purchases that they regret in hard times. Moreover, under the Second Circuit's reading of the Act, Tenants could unilaterally set aside the Garage Lease even if there had been an enormous escalation in the price of the units and a sharp decrease in the cost of maintenance and taxes.

D. The Present Suit Involves No Distinction Between Tenants Who Purchased From Associates and Those Who Purchased From Prior Unit Holders

Finally, it is wholly irrelevant that some tenants did not purchase their units from Associates, but from other unit holders. (Respondent's Brief at 25-26) If subsequent purchasers have any grievances, they should be directed toward the sellers of their respective units, not toward Associates.

When all these irrelevancies are put into perspective, its is clear that Tenants has not demonstrated that there are any factual issues that argue against review or that should predispose this Court to award Tenants dispensation from the ordinary rules of commercial transactions or statutory construction. The long list of District Court cases cited by Tenants as following the Second Circuit

(Respondent's Brief 32-34) is not testimony to the wisdom of the Second Circuit's decisions, but only to the binding power of those decisions on the District Courts within the Circuit.

The Second Circuit has vastly expanded a statute that Congress plainly intended to have a narrow scope. The important issue before this Court is whether the federal courts should have the power to construe statutes in complete disregard of Congressional intent and in violation of well established principles of statutory construction solely to achieve a result that the court, but not Congress, deems appropriate.

CONCLUSION

For the reasons stated in Petitioners' original Petition, the Writ of Certiorari should be granted to correct serious mistakes in the construction of section 3607 of the Condominium and Cooperative Abuse Relief Act.

Respectfully submitted,

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